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The Manufacturers Hanover
Financial Digest
Weekly Commentary, Selected Financial Data, and Business Indicators

MONDAY, JUNE 17, 1985. VOLUME XXII, NUMBER 24

The Consumer . . .

Over the past several months, the growth rate of the inflation-adjusted Gross National Product (GNP) has slowed to a crawl, prompting some analysts to believe that recession may be near at hand. But a recession is unlikely—at least in the near term. To be sure, the economy has developed many soft spots, largely due to competition from low-priced imports. But real domestic demand—real GNP less net exports—expanded by a solid four percent in the first quarter compared with 1984's fourth, and its continuing growth should keep the 31-month old recovery moving forward throughout the year.

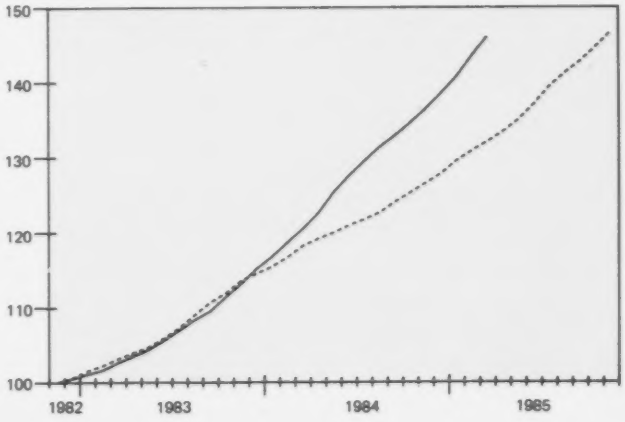
Since consumer spending accounts for nearly two-thirds of GNP, consumer behavior is the key to the economy's performance. And while the outlook for this sector is far from certain, it is more optimistic than the recent numbers suggest. Retail sales have been bumpy since the beginning of this year, posting two monthly declines since January. However, over the past two months, retail sales have been advancing at a nearly nine percent annual rate—despite May's decline—up considerably from the six percent annual rate of rise posted in the first quarter.

Nevertheless, the year-over-year increases have tapered off and retail sales levels are currently only 5.3 percent higher than at this time last year. Just why consumers are holding back on purchases is unclear, because they seem to be well positioned to keep spending at a good pace. For one thing, Americans are enjoying the lowest interest rates in at least five years, with auto loan and mortgage rates now sharply lower. Meanwhile, their buying power continues to improve as inflation remains subdued.

. . . Appears Able And Willing . . .

For another, the job market is strong. More than 1.4 million jobs have been created in the first five months of the year and the Conference Board's Help Wanted Advertising Index is currently more than 11 percent higher than last year. The manufacturing sector has been adversely hurt by foreign competition, but the service sector continues to generate strong job growth. Furthermore, two important industries are still exhibiting a fair amount of strength. Both domestic new-car sales and residential construction are still on the rise. Detroit is selling new cars at an 8½ million unit annual rate so far this year, up from 7.4 million six months ago. During the ten days ending on June 10, domestic producers sold the most cars for this period in five years. Housing starts have climbed by more than 22 percent in the past six months and are running at a solid 1.9 million unit pace—their highest level in over a year.

CONSUMER INSTALLMENT CREDIT OUTSTANDING
CURRENT RECOVERY (LINE), AVG. OF 5 PREVIOUS RECOVERIES (DOT)
(TROUGH=100)



One possible explanation for the more subdued spending pace of the first quarter may be the Internal Revenue Service's well-publicized delays in processing individual income tax refunds earlier this year. With billions of dollars withheld from consumers, some belt tightening may have occurred until refunds arrived. Another reason could be the consumers are waiting for deeper price markdowns. At the end of last year, it was the promotional atmosphere which drew people back to stores.

On the brighter side, there was some benefit to the earlier slowdown in consumer spending. While buyers tightened their purse strings, after-tax incomes jumped at a seven percent annual rate in the first four months of the year. As a result, they were able to replenish their savings accounts, causing the savings rate to rebound to a healthy 5.9 percent of disposable income in April from 3.8 percent in March.

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Spending by consumers is usually influenced by their perceived near-term outlook for the economy in general, and their employment and income prospects in particular. It is thus good to know that the most recent survey conducted by the University of Michigan shows that consumer sentiment is still rosy and buying plans—especially for cars and housing—remain strong. This positive outlook has been underscored by the rapid accumulation of installment debt by consumers. It has expanded by more than 45 percent since the end of the last recession—sharply above the average 32 percent increase posted at this point in the five previous recoveries (see chart on page 1). In the last four months, consumers have taken on an average of $8 billion of new debt per month, but in so doing, boosted the ratio of outstanding installment debt-to-disposable income to 18.1 percent—surpassing the record levels seen in the late 1970s. Then the "buy now before prices go up" psychology prevailed, sending consumers off on a buying and borrowing binge in order to protect themselves against that era's rapid escalation of prices.

. . . To Keep The Expansion Going

Whereas in the past the upward climb of this ratio would have suggested that consumers were getting overextended, this time it may not pose as serious a threat as it once did. Like income, consumers' wealth is also a crucial determinant of consumption patterns. Since the end of the last recession, household financial assets which include demand deposits,

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 6/12/85	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	175.013	+ 1.369	+11.744
Loans to Depository Inst.	.819	– 1.042	– 1.689
Float	1.026	+ .882	+ .556
Total Reserve Bank Credit	188.796	+ 1.530	+14.271
Treasury Deposits with Federal Reserve Banks	2.077	– .323	– 1.234
Currency in Circulation	185.552	+ .645	+11.138
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	120.826	– 1.377	+ 5.380
	6/5/85		
Member Bank Reserves:			
Total Reserves Held	40.630	– .094	+ 4.065
Excess (Deficiency)	.844	– .014	+ .358
Net Free Reserves	.240	+ .447	+ 2.808
		% Change Since Three Months Ago*	**% Change Since Year Ago**
Monetary Aggregates †			
M1 (6/3/85)	585.6	+ 8.5‡	+ 7.2‡
M2 (May '85)	2,442.2	+ 3.8	+ 8.4
M3 (May '85)	3,077.4	+ 4.8	+ 9.3
Domestic Nonfinancial Debt (1st Q'85)	6,147.0	+ 11.3	+ 13.6

†Seasonally adjusted. * Seasonally adjusted annual rate. ‡ Four-week moving average.

New York Money Market

Offering Rates 6/14/85	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	6.60%	6.85%	7.00%
* Federal Agencies	7.00	7.50	8.00
* Municipal Notes—High Grade (46% Taxable Equivalent)	7.69	7.69	7.87
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.40	7.45	7.75

‡Finance Company Paper—Prime

5- 14 days	7.38%
15- 29 days	7.38
30- 59 days	7.38
60- 89 days	7.38
90-179 days	7.38
180-239 days	7.40
240-270 days	7.40

‡* Bankers' Acceptances

Jul.	7.30%
Aug.	7.30
Sep.	7.30
Oct.	7.30
Nov.	7.30
Dec.	7.30

‡Industrial Paper—Prime

30- 89 days	7.25%
90-120 days	7.13

†Federal Funds Effective Rate 7.40%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	1st Q'85	$ 3,817	$ 3,759	$ 3,553
Gross National Product (1972 Dollars)*	1st Q'85	$ 1,665	$ 1,662	$ 1,611
Percent Change, Annual Rate	1st Q'85	0.7	4.3	10.1
Change in Consumer Prices*	Apr '85	4.8%	6.0%	4.8%
Change in Producer Prices*	May '85n	2.4%	3.6%	– 1.2%
Civilian Employment (Thousands of Persons)†	May '85	106,960	106,945	105,162
Unemployment as % of Civilian Labor Force†	May '85	7.3%	7.3%	7.5%
Personal Income*	Apr '85	$ 3,174	$ 3,156	$ 2,969
Leading Indicators Composite Index (1967=100)†	Apr '85	167.4	167.7	168.1
Industrial Production Index (1967=100) †	May '85n	165.3	165.5r	162.8
Net Change in Consumer Installment Credit †	Mar '85	$ 8.34	$ 9.04	$ 5.93
U.S. Merchandise Trade Balance †	Apr '85	–$ 11.85	–$ 11.05	–$ 11.88
Plant and Equipment Expenditures*	3rd Q'85n	$392.61(a)	$385.31(a)r	$361.12
Private Housing Starts (Thousands of Units)*	Apr '85	1,913	1,883	1,949
New Construction Expenditures*	Apr '85	$ 325.7	$ 322.4	$ 308.6
Total Business Inventories †	Apr '85n	$ 581.3	$ 578.8r	$ 545.9
Total Business Sales †	Apr '85n	$ 425.7	$ 420.8r	$ 408.3

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

savings accounts, stocks and bonds have soared by more than $1 trillion (about one-quarter of which was due to rising stock prices). At the same time, total household debt, which includes mortgages as well as installment debt and outstanding loans, rose only half as much.

Thus, with incomes and assets growing, even the hefty acquisition of mortgage and installment debt in recent months does not necessarily indicate that a retrenchment by consumers is at hand. In fact, they now own $2.21 of financial assets for each dollar of debt outstanding, or ten percent more than at the early 1980 low point. And if the assets-to-debt ratio would fall to the early 1980 level, consumers could borrow for another 10 months at this year's breakneck pace—even if there were no additional financial asset accumulation.

Finally, another important consideration is the changing demographic composition of Americans in general, and the maturation of the "baby-boom" generation in particular. This group has now entered into the high spending and borrowing years. And, according to the Federal Reserve's survey of consumer finances, 55 percent of the people in this age group have outstanding installment debt compared with only 29 percent of those in other age brackets. Similarly, about 85 percent of them are paying off a mortgage, compared with only 40 percent in the other age groups. H

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (5/29/85)	155,625	– 337	+ 2,208
New York City (6/5/85)	33,530	+ 263	+ 264
Commercial Paper (6/5/85)	260,203	+ 147	+43,924

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (5/29/85)	253,640	– 747	+ 11,675
New York City (6/5/85)	61,794	+ 375	– 2,324

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (5/29/85)	670,492	– 3,423	+ 56,895
New York City (6/5/85)	151,388	+ 5,587	+ 13,023

Financial Markets

	Friday 6/14/85	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	6.84%	– .54	– 3.41
180-Day Bills†	7.17	– .46	– 3.88
Longest Bills†	7.49	– .50	– 4.36
Recent Issues:			
9⅛s 5/31/87	8.40	– .39	
11¼s 3/31/89	9.19	– .30	
11¼s 5/15/95	9.90	– .29	
11¼s 2/15/15	10.30	– .23	
Municipals:			
Bond Buyer–20 Bond Index* (6/13/85)	8.66%	+ .06	– 1.93
Blue List Total ($ Million)	$2,130	+$ 352	+ $1,048
30-Day Visible Supply ($ Million)	$2,269	–$1,251	+ $ 273
Total	$4,399	–$ 899	+ $1,321
Corporates:			
Moody's Aa Composite (6/13/85)	11.48%	+ .05	– 2.78
30-Day Visible Supply ($ Million)	$ 818	–$ 160	+ $ 528
Stocks:			
Dow-Jones Averages:			
Industrials	1,300.96	– 28.68	+ 214.06
Transportation	636.94	– 22.89	+ 178.92
Utilities	164.60	+ .77	+ 42.30
65 Stocks	536.93	– 11.17	+ 113.03
Standard and Poor's 500 Stocks	187.10	– 2.58	+ 38.07
N.Y.S.E. Composite Index	108.56	– 1.41	+ 22.39
N.Y.S.E. Avg. Daily Vol. for Week (000's)	97,726	–22,724	+ 20,354

* 46% Taxable equivalent 16.04%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 6/14/85	Week Ago
Overnight	7.25%	7.50%
1 month	7.63	7.50
3 month	7.63	7.56
6 month	7.81	7.75
1 year	8.25	8.13
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	10.10%	10.05%
Long Term (7 to 15 yrs.)	10.60	10.55

FOREIGN EXCHANGE SPOT RATES

New York Opening (6/14/85)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.01627	61.4800
Canada	.7298	1.3703
Denmark	.09013	11.0950
France	.1076	9.2950
Germany	.3271	3.0575
Italy	.0005140	1945.50
Japan	.004020	248.78
Mexico	.003419	292.50
Netherlands	.2906	3.4440
Switzerland	.3887	2.5725
U.K.	1.2825	.7797

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